

Financial Literacy- An Essence of Financial Inclusion

Palak Mehta

Abstract

According to Bernanke: "Helping people better understand how to borrow and save wisely and how to build personal wealth is one of the best things we can do to improve the well-being of families and communities." The frequently overlooked poor also require a range of financial services like opportunities to earn, to protect the income earned, credit facilities, risk avoiding services like insurance, transfer of money etc. Poor families are not able to obtain wealth primarily because of two reasons, first being the absence of proper financial services (financial inclusion) and second being the dearth of knowledge of finance (financial illiteracy). Financial inclusion has come up as a preference for policy makers and regulators across the world in the war against poverty. Financial Literacy is the most essential part of the financial inclusion, as without having the knowledge of the basics the disadvantaged people would remain to be innocent and careless. Financial Literacy would encourage these people to save, access credit, usage of the funds, earn income to get a better livelihood and therefore become a part of the mainstream from the exclusion. This paper highlights the initiatives taken by the Indian banks to attain the financial inclusion in the country, the role of financial education in reducing the financial exclusion and promoting financial inclusion in the country.

Keywords: Financial Inclusion, Financial Education, Financial Literacy, Indian Banks

Financial Literacy

OECD (Organization for Economic Cooperation and Development) describes Financial Literacy as a mix of financial awareness, skills, knowledge, attitude and behavior required to make important financial decisions and eventually accomplish individual financial well-being. People attain financial literacy through a mechanism of financial education.

OECD describes Financial education as " the method by which financial consumers / investors enhance their knowledge of financial products, concepts and risks, instruction and objective advice, cultivate the skills and confidence to become more conscious of financial risks and opportunities, to make proper choices, to understand where to go for help and to take productive actions to enhance their financial well-being."

According to Sanchayan financial literacy is a broad issue, which can:

- Assist the poor and disadvantaged people to gradually move out of poverty.
- Youth and children to gain knowledge of the fundamentals that will last for a longer period.
- Adults to take proper financial decisions at each point of time.

It gives awareness and knowledge of financial market products, in order to make proper choices. An individual normally has definite resources and skills to acknowledge the complicatedness of financial dealings with financial intermediaries on a regular basis. Therefore financial literacy is the ability to understand, check and efficiently use financial resources that will help the individual to improve the well-being and security of himself, his family and his business.

Importance of Financial literacy

Here the main question is, " If a person has no idea for what he needs money for or how to use it, how the products and services would solve the purpose of that person?" Financial literacy gives the knowledge, skills and confidence to profitably carry out the financial transactions faced in everyday life. It involves the ability to know the financial choices, plans for the future, spend carefully and handles the challenges related with the life events such as job loss, retirement savings, expenses for a child's education. The OECD dedicated a chapter of its 2005 publication to the significance of financial education for bringing the people who don't have bank accounts and undeserved into the financial system. The OECD pointed various direct and indirect advantages for the unbanked:

- Enhanced knowledge of mainstream financial services and support to refrain non-standard services.
- Proper knowledge of risks and advantages of financial services such as credit.
- Less cost of information search for the unbanked
- More household savings
- Safeguard against immoral, unfair practices such as predatory lending
- Less cost of money transfers

Financial Inclusion

Financial inclusion by way of access to formal financial system is very important for the economic upliftment of the common man. It can be defined as the delivery of the banking and financial services at a reduced cost to the people who don't have an access to the financial services and also belonging to the low-income groups. Though credit is the most significant element, financial inclusion includes different financial services such as savings, insurance, payments and remittance facilities by the formal financial system. Commercial banks operating in the region are the providers of such facilities.

Financial Inclusion and the Indian Banks

The increasing global focus on the financial inclusion shows the concern of governments and central banks by bringing the people into the banks and financial services are provided to them. The main target of the inclusion effort is the unorganized sector, which continues financially excluded by enlarge. Hence it is difficult to cover, the size of the business provided by the sector is commercially not important, the broadly scattered nature and small individual needs provide services to the sector not feasible; the economic value addition by the sector is not high and therefore loans provided would turn into non-performing assets due to high default rates.

The commercial banks in India are presumed to be profitable in their trade as they are the chief protectors of the wealth of the citizens of India. At the same time the apex bank, ie. Reserve Bank of India has been circulating guidelines to the commercial banks to encourage the process of financial inclusion throughout India, with main focus on the states, which are economically underdeveloped. Therefore the commercial banks will play a dual role. On the one hand it has to raise its profitability and on the other part it is also predicted to serve a social cause by bringing the poor and unimportant people into the financial circle. It has become mandatory for the commercial banks to expand their range, offer different types of products to the poor and marginalized and continue profitable at the same time.

RBI has allowed and suggested the use of some other channels of encouraging financial inclusion to the commercial banks such as including the Self Help Groups (SHGs), Micro-finance institutions (MFIs), Regional Rural Banks (RRBs), Non-Commercial Banks such as National Bank for Agriculture and rural development (NABARD), Non Governmental Organizations (NGOs), Joint Liability Groups (JLGs), Co-operatives and Co-operative banks. Other companies in the financial sector such as Non- Banking Finance Companies (NBFCs), Mutual Fund companies and insurance companies will play a key role in the method of financial inclusion throughout India. Now commercial banks are involved in selling of financial products such as insurance, mutual funds, stocks and derivative products. Therefore it is quite clear that banks have taken the marketing position of the insurance companies. Delivery of banking services now actually mean the delivery of all types of financial services to the poor and marginalized in alliance with the other companies.

Financial Inclusion Initiatives

In order to provide growth momentum to the key sectors of an economy and mainly to insure access to economical financial services to the low-income class in the country, the Reserve Bank of India circulated different instructions to the banks to bring in comprehensive growth through financial inclusion like:

- To open ' No-Frills' saving accounts with less or nil minimum balance and also the charges for opening and managing the account.
- Relax ' Know Your Customer' (KYC) norm for opening a bank account with self-declaration of address and introduction by an account holder of a bank in order to expand the outreach of the bank accounts to the low income people.
- In order to insure smooth credit flow to the individual recipients of the rural families banks have been asked to propose ' General Purpose Credit Cards' facility. The holder of these cards will be entitled to credit up to 25,000 on revolving credit system basis at their rural and semi-urban branches.
- Banks were advised to adopt a easy system for one time settlement of overdue loans up to Rs 25,000. Moreover banks were asked that the responsible beneficiary shall be considered fit for fresh credit after one time settlement.
- In order to attain greater degree of " Financial Inclusion" banks were permitted to effectively use the services of Non-governmental organizations (NGOs), Micro-Finance Institutions, Self-Help Groups (SHGs) etc.

A strategy was made to attain the financial inclusion in the country. Banks were assigned the districts and were instructed to attain “Full Financial Inclusion” in the recognized districts by opening ‘ No-Frills Accounts and issuance of GCC etc.

Causes of Financial Exclusion and Role of Financial Education

- **Regulatory Constraints:** Some national regulatory frameworks restrict the ability of the financial providers to draw the attention of the new clients. The rules of KYC may unjustifiably affect the supply of the products to youth and migrant workers.
- **Infrastructure and Connectivity Barriers:** New solutions to financial inclusion are reliant on technology like mobile phones, computers etc. The groups where hardware is short in supply, electricity is unavailable, networks are limited are likely to be excluded.
- **Geographical and Physical Barriers:** Opening branches in the rural or low-profit areas is not a feasible option for the banks. Due to the poor infrastructure banks face difficulties in sending and storing cash in remote branches which decrease the productive supply of financial services.
- **Exclusionary Actions of Service Providers:** It involves charging high fees for transactions, need of high minimum balance, avoiding access to those with no credit card etc.

Various Demand Side Factors that lead to Exclusion are:

- **Low level of Financial literacy:** Lack of knowledge of various types of financial products, poor understanding of their use and likely costs, decrease the demand for relevant products.
- **Cultural and Physiological Barriers:** Personal and Cultural preferences and religious thoughts can restrict the number of financial products an individual demands. Lack of faith in financial service providers can create a hurdle to financial inclusion.
- **Linguistic and Educational Barriers:** Large number of population. Various languages and cultures with illiteracy play as a big stumbling block to financial inclusion. The challenge is to make the people financially literate.
- **Reduced Social and Technological Inclusion:** Lack of awareness of the technology such as use of ATM, Internet, mobile banking will create a hurdle to access the financial products. Biasness against certain groups based on caste, status, income, gender, language etc. has also been recognized as a hurdle to financial inclusion.
- **Financial Vulnerability Caused by Personal Circumstances:** Shortage of money, no credit history, unemployment and low income creates a hurdle to access financial products. In such situations people often move to informal service providers like moneylenders for their financial requirements, which further move them into poverty.

Financial Education Policies for Financial Inclusion

The rising global interest in financial education for financial inclusion is visible in national policies, framed to handle both demand and supply side barriers to financial inclusion and reduced levels of financial literacy. India clearly connects financial education and financial inclusion at all points of its draft National Strategy for Financial Education, saying that its mission is to ‘ initiate large finance education campaigns to support people to manage money more efficiently to attain financial well-being by accessing relevant financial products and

services through governed entities with fair and clear machinery for consumer protection and grievance redressal'. (Reserve Bank of India and Securities and Exchange Board of India, 2012).

RBI has recommended banks that there should be at least one Financial Literacy Centre in all the districts (640+) throughout the country. These centers need to conduct outdoor financial literacy camps at least once in a month. So far the banks have developed 650 FLCs. Moreover every rural branch (35000+) needs to conduct a financial literacy camp at least once in a month.

Conclusions and Suggestions

Financial Inclusion and Financial Literacy are related to each other. They are two components of integral strategy. Financial inclusion gives access and financial literacy gives awareness. The focus of the strategy at the fundamental level is to make people aware of the basic financial products, as it would be a challenge to connect large number of financially excluded people to the formal financial system. Disadvantaged people require access and awareness of financial services. For this purpose the focus of the financial literacy should be mainly directed towards distribution of easy messages of financial diligence in a native language through huge campaigns across the country linked with vigorous role out of financial inclusion plans by banks, insurance, pension funds and others. The strategy should be comprehensive- vigorous involving individuals, financial sector regulators, NGOs, financial sector companies, various international players and Central and State Government.

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Palak Mehta, Assistant Professor, School of Management, ITM University, Gurgaon, Haryana, India